

***United States Court of Appeals  
for the Second Circuit***



**APPENDIX**





# No. 75-6066

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IN THE  
**United States Court of Appeals**  
FOR THE SECOND CIRCUIT

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SECURITIES INVESTOR PROTECTION CORPORATION,  
*Applicant-Appellant,*  
SECURITIES AND EXCHANGE COMMISSION, *Plaintiff,*

v.

MORGAN, KENNEDY & Co., Inc.;  
IRWIN RUDNET AND GERALD RUDNET, *Defendants-Appellees.*

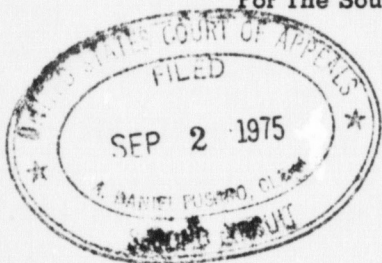
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CLAIM OF READING BODY WORKS, INC.  
PROFIT SHARING PLAN TRUST, *Claimant-Appellee.*

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On Appeal From the United States District Court  
For The Southern District of New York

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## APPENDIX

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THEODORE H. FOCHT  
*General Counsel*  
SECURITIES INVESTOR PROTECTION  
CORPORATION  
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Suite 800  
Washington, D.C. 20006  
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## *Docket Entries*

### **List of Relevant Docket Entries**

- March 9, 1973—Filed Application of Securities Investor Protection Corporation
- March 14, 1973—Filed Order Appointing Eugene L. Bondy, Jr. as Trustee for the Liquidation of Morgan, Kennedy & Co., Inc.
- September 10, 1974—Filed Application of Eugene L. Bondy, Jr. for Order to Designate the Claim of the Trustees of Reading Body Works Profit Sharing Plan
- October 16, 1974—Filed Application of Charles M. Solomon for Order to Designate Claim of Trustees of Reading Body Works, Inc.
- November 29, 1974—Filed Affidavit of William Ragusin, Liquidator of Morgan, Kennedy & Co., Inc.
- January 21, 1975—Entered Memorandum Opinion of Bankruptcy Judge Babbitt Designating Claim of Trustees of Reading Body Works Profit Sharing Plan
- February 14, 1975—Entered Order of Judgment of Bankruptcy Judge Babitt
- February 21, 1975—Filed Notice of Appeal of Securities Investor Protection Corporation to the District Court
- March 3, 1975—Filed Appellant's Designation of Contents of Record and Statement of Issues
- March 7, 1975—Filed Appellee's Designation of Contents of Record
- June 10, 1975—Filed Memorandum and Order of District Judge Marvin E. Frankel
- July 14, 1975—Filed Notice of Appeal of Securities Investor Protection Corporation to the Court of Appeals



IN THE  
**United States Court of Appeals**  
FOR THE SECOND CIRCUIT

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No. 75-6066

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SECURITIES INVESTOR PROTECTION CORPORATION,  
*Applicant-Appellant,*  
SECURITIES AND EXCHANGE COMMISSION, *Plaintiff,*

v.

MORGAN, KENNEDY & CO., INC.;  
IRWIN RUDNET AND GERALD RUDNET, *Defendants-Appellees.*

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CLAIM OF READING BODY WORKS, INC.  
PROFIT SHARING PLAN TRUST, *Claimant-Appellee.*

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On Appeal From the United States District Court  
For the Southern District of New York

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**APPENDIX**

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1

*Application of Eugene L. Bondy, Jr.*

UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

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73 Civil 1057 (RB)

SECURITIES INVESTOR PROTECTION CORPORATION, *Applicant*,  
SECURITIES AND EXCHANGE COMMISSION, *Plaintiff*,  
against

MORGAN, KENNEDY & CO., INC.;  
IRWIN RUDNET AND GERALD RUDNET, *Defendants*.

STATE OF NEW YORK,  
COUNTY OF NEW YORK, ss:

**Application**

EUGENE L. BONDY, JR., being duly sworn, deposes and says:

1. On March 13, 1973, by Order of the Honorable Marvin E. Frankel, United States District Court Judge for the Southern District of New York, I was appointed Trustee ("Trustee") for the liquidation of the business of Morgan, Kennedy & Co., Inc. (the "Debtor"), with all the duties and powers of a trustee prescribed in the Securities Investor Protection Act of 1970 (the "1970 Act").

2. This Application is being made for an Order (the form of which is annexed hereto) which would:

(a) designate the claim of the Trustees of the Reading Body Works, Inc. Profit Sharing Plan Trust (the "Trust") against the Debtor for \$133,051.15 to be the individual claims of the 108 individual beneficiaries of the Trust; and

*Application of Eugene L. Bondy, Jr.*

(b) order that under § 6(c)(2)(A)(ii) of the 1970 Act each of the individual beneficiaries of the Trust is a separate "customer" and thus entitled to the \$20,000 maximum coverage provided for in § 6(f) of the Act.

3. This Application also seeks an Order (in the form annexed hereto) to make an interim advance of \$20,000 to the Trust pending a final decision of the Trust's entire \$133,051.15 claim.

4. On April 5, 1957 the Reading Body Works, Inc. (the "Company") established the Reading Body Works, Inc. Profit Sharing Plan (the "Profit Sharing Plan"). Thereafter, on April 12, 1957, the Company and three individual Trustees ("the Trustees") entered into an Agreement and Declaration of Trust for the benefit of the individual employees of the Company.

5. Under the terms of the Profit Sharing Plan, yearly contributions are made by the Company to the Trust for the benefit of the Company's employees based upon the Company's yearly net earnings. Each employee accumulates "credits" or a percentage interest in the fund according to his (or her) annual compensation level and consecutive years of service. The Agreement and Declaration of Trust specifically require that a separate "account" be maintained for each employee to which is credited his proportionate share of the Company's yearly contribution and any increase in the market value of the trust fund. Each employee is given a non-forfeitable vested interest in the amounts allocated to his account which is received, according to certain conditions upon the termination of employment with the Company.

6. The Trust became a customer of the Debtor in December, 1972 as part of the transfer of customer accounts from Monaghan & Company, Inc., a broker-dealer whose business had been acquired by the Debtor. The

*Application of Eugene L. Bondy, Jr.*

Trust's account was handled by Frederick Garfinkle, a registered representative associated with the Debtor.

7. During the months of January and February of 1973 the Trustees authorized the Debtor to execute the sales of certain securities on behalf of the Trust. These securities were delivered to the Debtor in order to complete these sales. However, although the sales were completed by the Debtor, no part of the proceeds from them were ever paid to the Trust. The net proceeds from such sales totaled \$83,051.15, and this amount was credited to the account of the Trust on the books and records of the Debtor. On March 9, 1973, the filing date of this liquidation proceeding, these securities were being held by the Chemical Bank for clearance and transfer and efforts to recover them by the Trust have thus far been unsuccessful.

8. On February 7, 1973 the Debtor purchased, with free credit balance funds belonging to the Trust, a United States Treasury bill in the face amount of \$50,000. This treasury bill was fraudulently and illegally hypothecated with the Chemical Bank and its proceeds, which were credited against the Debtor's loan account by the Chemical Bank were never received by the Trust.

9. By reason of the foregoing, a credit balance in the amount of \$133,051.15 was owing to the Trust on March 9, 1973, the date of bankruptcy of the Debtor. (A copy of the Trust's customer account statement for March, 1973 is annexed hereto as Exhibit A).

10. By complaint dated June 7, 1973, the Trustees brought an action against the PBW Stock Exchange, Inc., the Chemical Bank, Irwin Rudnet, Gerald Rudnet, and Frederick Garfinkle, seeking to recover the above amount. This action was based upon alleged violations of the law committed by the persons named in the complaint. At this date, no recovery has been had in this action by the Trust.



*Application of Eugene L. Bondy, Jr.*

11. By letter dated June 26, 1973 counsel for the Trustees made formal claim upon the Debtor on behalf of each of the beneficiaries of the Trust. The Claim (a copy of which is annexed hereto as Exhibit B), dated June 20, 1973, asked for money balances as of March 9, 1973 in the amount of \$133,236.15.\* Attached to the claim was a memorandum (a copy of which is annexed hereto as Exhibit C) which sets forth the individual transactions, including that concerning the proceeds of the \$50,000 face amount treasury bill, which gave rise to the claim.

12. By letter dated October 9, 1973 (a copy of which is annexed hereto as Exhibit D), the Trustees informed the Securities Investor Protection Corporation ("SIPC") that he considered each of the 108 beneficiaries of the Trust a separate "customer" within the meaning of § 6(c)(2)(A)(ii) of the 1970 Act and therefore each entitled to the maximum dollar limitation provided in § 6(f) thereof. The Trustee based his conclusion in part upon a memorandum of law which had been prepared by his counsel (a copy of which is annexed hereto as Exhibit E).

13. On March 6, 1974 William Ragusin, the liquidator of the Debtor, on behalf of the Trustee, filed a Proof of Claim with the Insurance Company of North America ("INA") making claim under a broker's blanket bond which had been maintained by the Debtor. This claim alleged that the failure of the Debtor to pay the proceeds of the \$50,000 treasury bill to the Trust was the direct result of the illegal and fraudulent conduct of certain of the employees of the Debtor and that therefore the Trustee should be reimbursed by INA under the terms of the broker's blanket bond for the loss resulting from this dishonest conduct. INA is now investigating this claim

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\* The \$181 difference between this figure and the amount of the advance sought by the Trustee results from a revision of the Trust's initial estimate of the value of the \$50,000 treasury bill.

*Application of Eugene L. Bondy, Jr.*

but has thus far given no indication of an intention to pay it.

14. By letter dated May 22, 1974 counsel for the Trustee sent a Trustee's Request for SIPC Advance for Payments to Customers dated May 17, 1974 (a copy of which is annexed hereto as Exhibit F), to SIPC requesting an advance in the amount of \$133,051.15. This request was based upon the Trustee's previous position that each of the 108 individual beneficiaries of the Trust should be considered a separate customer under § 6(c)(2)(A)(ii). Counsel for the Trustee also requested that if SIPC decided to deny the request for the full amount, it forward \$20,000 in cash as an interim advance. There is no dispute between SIPC and the Trustee that the Trust is entitled to at least \$20,000 in satisfaction of its claim.

15. By letters dated May 23, 1974 and June 10, 1974 (copies of which are annexed hereto as Exhibits G and H), counsel for SIPC informed the Trustee that it would not treat the claim of the Trust as the claim of 108 separate customers of the Debtor and therefore would not advance the full amount of the Trust's claim.

16. By letter dated June 28, 1974 (a copy of which is annexed hereto as Exhibit I), Thomas R. Cassella, a manager of operations associated with SIPC, returned the Request for Advance dated May 17, 1974 to the Trustee stating that the request had not been approved for payment. Mr. Cassella also stated that a separate court order would be necessary before the \$20,000 interim payment could be advanced.

17. The Trustee has given careful consideration to the claim of the Trust and has determined after reviewing the advice of his counsel contained in the memorandum of law dated October 5, 1973 (Exhibit E) as well as the letter stating the position of SIPC dated May 23, 1974,

*Application of Eugene L. Bondy, Jr.*

(Exhibit G), that the individual beneficiaries of the Trust are each entitled to protection as individual customers under the 1970 Act.

18. If the claim of the Trust is paid in full, every claim filed by a customer which has not been found objectionable by the Trustee and disallowed by a court order will have been satisfied in full.

19. The Trustee believes that the spirit of the 1970 Act and the interests of justice require that this claim be paid. The beneficiaries of the Trust are factory workers whose savings make up the funds which were invested by the Trust. Congress was concerned with protecting this very class of small investors when it enacted the 1970 Act.

20. As it pointed out in the memorandum of law annexed hereto as Exhibit E, either the 1970 Act nor the series 100 rules promulgated thereunder by SIPC give a definite answer to the treatment to be accorded the beneficiaries of trusts under the 1970 Act. The Trustee feels that since the 1970 Act was to have the same purpose and effect as the Federal Deposit Insurance Act and the Federal Savings and Loan Insurance Act, and since the regulations promulgated under both of those acts provide separate protection for each beneficiary of a trust maintaining a deposit with an insured institution, the same kind of protection should be available to investors maintaining accounts with broker-dealers who have become insolvent.

Dated: New York, New York

September 5, 1974

/s/ EUGENE L. BONDY, JR.  
Eugene L. Bondy, Jr.

(Subscription omitted in printing)

**morgan, kennedy & co., inc.**  
Members: Philadelphia - Baltimore - Washington Stock Exchange

- 5 Hanover Sq New York, New York 10004 • (212) 247-1480
- Hitching Post Inn, Box 938 Chambersburg, Pa. 17201
- 301 Arthur Godfrey Rd., Miami Beach, Florida 33140

YOUR ACCOUNT NO. TYPE BAE  
32-00862 1 095

YOUR TAXPAYER  
IDENTIFICATION NUMBER

TTEES FOR READING BODY WORKS  
PROFIT SHARING PLAN  
DTD 4/12/57 SANAMETRICS  
420 GREGG AVE PO BOX 14  
READING PA 19003

PERIOD ENDING 03/30/73

PAGE # 1

DATE	DEBIT	CREDIT	DESCRIPTION	DEBIT	CREDIT	DEBIT	CREDIT
03/05/73			BAL FWD FEB 28 50M. USTEAS R	CR			83,051.15CR
			CLOSING BALANCE MAR 30			50,000.00	133,051.15CR
			POSITIONS				
03/30/73	200		HOFFMAN ELECTRONICS				
03/30/73	50,000		US-TREASURY BILL				
			5.40-DUE-3/1/1973				

IF THIS STATEMENT IS NOT CORRECT INDICATED  
ABOVE, PLEASE RETURN IT IMMEDIATELY

PLEASE RETAIN THIS STATEMENT FOR INCOME TAX  
PURPOSES. A CHARGE WILL BE MADE FOR ADDI-  
TIONAL COPIES.

"ANY FREE CREDIT BALANCE CARRIED BY MORGAN, KENNEDY & CO., INC. FOR YOUR ACCOUNT REPRESENTS FUNDS PAYABLE UPON DEMAND WHICH, ALTHOUGH PROPERLY ACCOUNTED FOR ON OUR BOOKS OF RECORD, ARE NOT SEGREGATED AND MAY BE USED IN THE CONDUCT OF OUR BUSINESS."



Application of Eugene L. Bondy, Jr.

EXHIBIT B

MORGAN, KENNEDY & CO., INC.  
IN LIQUIDATION UNDER THE SECURITIES INVESTOR PROTECTION ACT OF 1970  
EUGENE L. BONDY, JR., TRUSTEE

NOTE: THIS CLAIM FORM MUST BE COMPLETED AND FILED BY CUSTOMERS WHO HAVE CLAIMS  
FOR CASH OR SECURITIES, OR BOTH. IF NO CLAIM IS FILED BY JUNE 29, 1973  
THE TRUSTEE WILL ASSUME THAT THERE IS NO CLAIM.

32-00662  
32-11674  
Irving Suknow, Herbert Ostroff, and Doris  
Rauenzahn, Trustees for the Reading Body  
Works, Inc. Profit Sharing Plan Trust, on  
behalf of each beneficiary of the said Trust  
420 Gregg Avenue  
P.O. Box 14  
Reading, Pa. 19603

CUSTOMER CLAIM IN THE LIQUIDATION  
OF MORGAN, KENNEDY & CO., INC.,  
AS OF MARCH 9, 1973

JUN 29 1973

Change above if incorrect

Telephone: Area code 125 # 376-7103 or Social Security # Taxpayer Identification #

1. Claim for money balances as of March 9, 1973:  
Morgan, Kennedy & Co., Inc. owes me (Credit (Cr.) balance) \$ 133,236.15  
I owe Morgan, Kennedy & Co., Inc. (Debit (Dr.) balance) \$ None
2. Claim for securities as of March 9, 1973: (please check answer)  
Morgan, Kennedy & Co., Inc. owes me securities Yes ☒ No ☐  
I owe Morgan, Kennedy & Co., Inc. securities Yes ☐ No ☒  
If Yes, please list below (please attach  
additional sheets for more space if necessary):

Date of Transaction	Name of Security	Number of shares or par value bonds	
		Morgan, Kennedy & Co., Inc. owes me (Long)	I owe Morgan Kennedy & Co., Inc. (Short)
	(SEE ATTACHMENT)		

THE ABOVE CLAIM DOES NOT INCLUDE TRANSACTIONS AFTER MARCH 9, 1973.

3. Has there been any change in your account since March 9, 1973? Yes ☐ No ☒  
If yes, please give details by attaching a separate sheet.
4. Are you related to any officer, director, employee, registered  
representative or person affiliated with Morgan, Kennedy & Co., Inc? Yes ☐ No ☒  
If yes, specify relationship
5. Does anyone other than you or your spouse have a beneficial  
ownership in the above described account? Yes ☒ No ☐  
If yes, please identify by name and address such other person(s)  
and describe the extent of their ownership in a signed attach-  
ment to this claim.

(over)

Application of Eugene L. Bondy, Jr.  
EXHIBIT A

## Application of Eugene L. Bondy, Jr.

6. Are you an officer or director of Morgan, Kennedy & Co., Inc. or the beneficial owner of 5 per centum or more of any equity security (other than a non-convertible stock having fixed preferential dividend and liquidation rights) of that corporation? Yes \_\_\_ No X  
If yes, please explain in an attachment to this claim.
7. Have you ever filed a claim for securities or cash with any other trustee in a liquidation under the Securities Investor Protection Act of 1970? Yes \_\_\_ No X  
If yes, please furnish complete details in an attachment to this claim.
8. Have you authorized any person to execute transactions on your behalf on a discretionary basis for the above account? Yes \_\_\_ No X  
If yes, please furnish name of person \_\_\_\_\_

## THE FOREGOING CLAIM IS TRUE AND ACCURATE:

DATE:

SIGNATURES:

6/10/73

Eugene L. Bondy, Jr. Trustee

6/10/73

Donna K. Bondy Trustee

6/10/73

Richard E. Bondy Trustee

(If account is carried in more than one name, all must sign. If other than a personal account, please state your capacity and authority)

"Whoever knowingly and fraudulently presents any false claim for proof against the estate of a bankrupt or uses any such claim in any bankruptcy proceeding ... shall be fined not more than \$5,000 or imprisoned not more than five years, or both."

18 U.S.C. § 152

A legible copy of the following documentation should be forwarded to the trustee to support your claim and assist in its processing:

- last customer statement received, together with your comments on differences, if any
- a schedule describing how you determined the money balances and securities shown above
- purchase and sales confirmations covering the items shown above
- any other documentation which you believe would be of assistance in processing your claim such as cancelled checks, correspondence, receipts, etc.

This claim, together with supporting documentation, should be mailed promptly to:

Eugene L. Bondy, Jr., Trustee in the Liquidation of  
Morgan, Kennedy & Co., Inc.  
P.O. Box 5796  
Grand Central Station  
New York, N.Y. 10017

*Application of Eugene L. Bondy, Jr.*

EXHIBIT C

MORGAN, KENNEDY & Co., INC.

CUSTOMER CLAIMS OF

IRVING SUKNOW, HERBERT OSTROFF, AND DORIS RAUENZAHN  
("TRUSTEES") TRUSTEES FOR THE READING BODY WORKS,  
INC. PROFIT SHARING PLAN TRUST ON BEHALF OF EACH  
BENEFICIARY OF THE SAID TRUST

ATTACHMENT

*I. Summary of Claim*

The Trustees are making this claim on behalf of each of the beneficiaries of the Trust, numbering approximately 108 individuals. The Trustees assert that each beneficiary is a separate customer of Morgan, Kennedy & Co., Inc. ("Morgan") under the Securities Investors Protection Act of 1970 ("the Act"). The Trustees are acting as such pursuant to an agreement dated April 12, 1957, between them and Reading Body Works, Inc., a Pennsylvania corporation.

The claim includes the right to 200 shares of Hoffman Electronics which were delivered to Morgan solely for the purpose of registration.

The Claim also includes the rights of the Trustees and their beneficiaries relating to a series of transactions in which Morgan effected sales transactions of securities of the Trust and accepted the securities, but failed to complete the sales. The net proceeds of such sales totalled \$83,051.15. No part of such proceeds were ever paid to the Trust. The Trustees understand that Morgan diverted certain of the Trust's securities by pledging them for debts of Morgan instead of using them to complete the sales. The Trustees never authorized Morgan to hypothe-



*Application of Eugene L. Bondy, Jr.*

cate securities of the Trust. If any such securities are still in the possession of any such pledgee, and if they should be returned to Morgan, they will become specifically identifiable securities of the Trust.

To the extent such securities may not be specifically identifiable, the Trust has a securities claim for them with respect to each beneficiary of the Trust.

To the extent that any such securities, or other securities traceable to them, are in the possession of Morgan, they are specifically identifiable securities of the Trust. If they are not specifically identifiable, the Trust has a securities claim for them with respect to each beneficiary of the Trust.

To the extent that the Trust does not have a securities claim with respect to any such securities, it has a cash claim for the net proceeds of their sale.

The claim also includes the right to a \$50,000 U.S. Treasury Bill which Morgan purchased with the Trust's free credit balance funds. Morgan never delivered the Bill to the Trust. Instead, Morgan, without authorization, delivered the Bill to a bank as security for Morgan's debt to such Bank.

To the extent the Treasury Bill comes into the possession of Morgan, it will be a specifically identifiable security which belongs to the Trust.

If the Treasury Bill is not a specifically identifiable security, the Trust has a securities claim with respect to the Treasury Bill.

To the extent the Trust does not have a securities claim with respect to the Treasury Bill, it has a cash claim for its value at its maturity.



*Application of Eugene L. Bondy, Jr.*

*II. Hoffman Electronics*

On or about October 5, 1972, the Trust purchased 200 shares of Hoffman Electronics Corp through Monaghan & Company, Inc. ("Monaghan"), which carried them in street name. On or about February 8, 1973, Monaghan delivered the Certificate for such shares, No. NY/U-2668, to the Trust. On or about February 14, 1973, the Trust delivered the certificate to Morgan for re-registration in the name of the Trust. The Trust has never received a certificate in its name, nor the return of the certificate it delivered to Morgan.

Attached hereto are true copies of:

1. Monaghan's purchase advice, October 5, 1972.
2. Monaghan's letter of transmittal
3. Monaghan's statement, December 31, 1972.
4. Morgan's receipt for the certificate

*III. U.S. Treasury Bill*

On or about January 31, 1973, Morgan purchased for the Trust, with the Trust's free credit balance funds, a 5.40% U.S. Treasury Bill, CUSIP #912793-QH-2, due March 1, 1973. The Trust never received the Bill from Morgan. Instead, Morgan delivered the Bill to Chemical Bank in connection with the indebtedness of Morgan to such Bank. Morgan had no right to do so. Attached hereto is a true copy of Morgan's purchase advice dated January 31, 1973.

*IV. Other Securities*

1. *AT&T Convertible \$4.00 Preferred.* On or about February 13, 1973, the Trust sold through Morgan 400 shares of convertible \$4.00 preferred stock of American Telephone & Telegraph Company. The net proceeds of

*Application of Eugene L. Bondy, Jr.*

the sale were to have been \$24,097.41. Thereafter, the Trust delivered to Morgan AT&T's certificates 2201-8836 for 200 shares and 2907-6089 for 200 shares, solely for the purpose of completing the sale. Instead, Morgan, without any right to do so, delivered the certificates to Chemical Bank, apparently in connection with debt which Morgan owed to that Bank. The Trust has never received any of the proceeds of the sale. Attached hereto is a true copy of Morgan's sale advice dated February 13, 1973.

2. *AT&T Debenture, 7%, '01.* On or about February 13, 1973, the Trust sold through Morgan a \$10,000 debenture, 7%, 2/15/2001 of American Telephone & Telegraph Company. The net proceeds of the sale were to have been \$9,627.92. Thereafter, the Trust delivered to Morgan AT&T's debenture No. R100347, solely for the purpose of completing the sale. Instead, Morgan, without any right to do so, delivered the debenture to Chemical Bank, apparently in connection with debt which Morgan owed to that Bank. The Trust has never received any of the proceeds of the sale. Attached hereto is a true copy of Morgan's sale advice dated February 13, 1973.

3. *AT&T Debenture, 8¾%, '00.* On or about February 13, 1973, the Trust sold through Morgan a \$10,000 debenture, 8¾% 5/15/2000 of American Telephone & Telegraph Company. The net proceeds of the sale were to have been \$11,170.83. The Trust delivered to Morgan AT&T's debenture No. 8117-2906, solely for the purpose of completing the sale. Instead, Morgan, without any right to do so, delivered the debenture to Chemical Bank, apparently in connection with Morgan's debt to that Bank. The Trust has never received any of the proceeds of the sale. Attached hereto is a true copy of Morgan's sale advice dated February 13, 1973.

4. *PT&T Stock.* On or about February 13, 1973, the Trust sold through Morgan 900 shares of Pacific Tele-

*Application of Eugene L. Bondy, Jr.*

phone & Telegraph stock. The net proceeds of the sale were to have been \$15,821.88. Thereafter, the Trust delivered to Morgan PT&T's certificates 71S-61613 and NB 183601-08, solely for the purpose of completing the sale. Instead, Morgan, without any right to do so, delivered the certificates to Chemical Bank, apparently in connection with debt which Morgan owed to that Bank. The Trust has never received any of the proceeds of the sale. Attached hereto is a true copy of Morgan's sale advice dated February 13, 1973.

5. *Anaconda Corp.* On or about February 8, 1973, the Trust sold through Morgan 300 shares of Anaconda Corp. stock. The net proceeds of the sale were to have been \$6,351.82. Thereafter, the Trust delivered to Morgan, solely for the purpose of completing the sale, Anaconda's certificates N 56421 through N 564623 for 100 shares each. These certificates were cancelled by Anaconda's transfer agent on March 5, 1973, and new Anaconda certificates N 707401 through -03 for a like number of shares were issued to "Kenmorg," 5 Hanover Square, New York, New York. Instead of using the new certificates to complete the sale, Morgan delivered the new certificates to Chemical Bank, apparently in connection with Morgan's debt to that Bank. The Trust has never received any of the proceeds of the sale. The Trustees believe that Kenmorg is a nominee designation for Morgan, and that the shares, which belong to the Trust, are now registered in that name, the certificates being in the possession of Chemical Bank. Attached hereto are true copies of:

- a. Morgan's sale confirmation dated February 8, 1973
- b. Letter dated April 3, 1973 from First National City Bank, transfer agent for Anaconda.

6. *Itek Corporation.* On or about February 13, 1973, the Trust sold through Morgan 100 shares of Itek Corporation stock. The net proceeds of the sale were to have been



*Application of Eugene L. Bondy, Jr.*

\$4,331.31. Thereafter the Trust delivered to Morgan, solely for the purpose of completing the sale, Itek's certificate BC 19399. This certificate was cancelled by Itek's transfer agent and a new Itek certificate 21851 for a like number of shares was issued on March 8, 1973 to "Kenmorg," 5 Hanover Square, New York, New York. Instead of using the new certificate to complete the sale, Morgan delivered the new certificate to Chemical Bank, apparently in connection with Morgan's debt to that Bank. The Trust has never received any of the proceeds of the sale. The Trustees believe that Kenmorg is a nominee designation for Morgan, and that the shares, which belong to the Trust, are now registered in that name, the certificates being in the possession of Chemical Bank. Attached hereto are true copies of:

- a. Morgan's sale confirmation dated February 13, 1973
- b. Letter dated April 2, 1973 from The First National Bank of Boston, transfer agent for Itek.

7. *Syntex Corp.* On or about December 29, 1972, the Trust sold through Morgan 100 shares of Syntex Corp. stock. The net proceeds of the sale were to have been \$8,234.83. Thereafter, the Trust delivered to Morgan Syntex's certificate JC 106718, solely for the purpose of completing the sale. The Trust has never received any part of the proceeds of the sale. The certificate the Trust delivered to Morgan was cancelled by Syntex's transfer agent on February 21, 1973, and new Syntex certificates, 457430/1, were issued to "Kenmorg," 5 Hanover Square, New York, New York. Attached hereo are true copies of:

- a. Morgan's sale confirmation dated December 29, 1972.
- b. Letter dated May 2, 1973, from the Chase Manhattan Bank, transfer agent for Syntex.
- c. Letter dated June 1, 1973 from the Chase Manhattan Bank, transfer agent for Syntex.

*Application of Eugene L. Bondy, Jr.*

8. *Colorado Bancorp.* On or about February 13, 1973, the Trust sold through Morgan 500 shares of Commercial Bancorporation of Colorado stock. The net proceeds of the sale were to have been \$3,413.25. Thereafter, the Trust delivered to Morgan Colorado Bancorp.'s certificates AC 1887 through AC 1891, solely for the purpose of completing the sale. The Trust has never received any of the proceeds of the sale. The certificates the Trust delivered to Morgan were cancelled by Colorado Bancorp.'s transfer agent on March 2, 1973, and Colorado Bancorp.'s certificates AC 2020, AC 2022 and AC 2023, for 100 shares each, were issued to "Kenmorg," 5 Hanover Square, New York, New York. Other certificates were issued for the other 200 shares, being AC 2021 and AC 2019 or AC 2024, those shares being transferred out of Kenmorg on March 21, 1973. Attached hereto are true copies of:

a. Morgan's sales confirmation dated February 13, 1973.

b. Letter dated March 13, 1973 from Provident National Bank, transfer agent for Colorado Bancorp.

c. Letter dated April 19, 1973 from Provident National Bank, transfer agent for Colorado Bancorp.

*V. Cash Reconciliation*

Attached hereto is a summary of the transactions between Morgan and the Trust which show a computation of the cash debt of \$133,236.15.

*VI. Identification of Beneficiaries*

As of Mar. 9, 1973, the Reading Body Works, Inc. Profit Sharing Plan Trust had approximately 108 beneficiaries. Their names, their positions at Reading Body Works, Inc., and the percentage allocated at that time to each of them, is shown on a schedule attached.

*Application of Eugene L. Bondy, Jr.**VII. Reservation of Rights*

The filing of this claim is not intended to, and shall not operate so as to effect any waiver, impairment, or delay in the rights of the Trustees to proceed against parties other than Morgan with respect to the rights of the Trust described herein.

/s/ IRVING SUKNOW  
Irving Suknow

/s/ DORIS RAUENZAHN  
Doris Rauenzahn

/s/ HERBERT OSTROFF  
Herbert Ostroff

*Application of Eugene L. Bondy, Jr.*

## EXHIBIT F

## SECURITIES INVESTOR PROTECTION CORPORATION

TRUSTEE'S REQUEST FOR SIPC ADVANCE PAYMENTS TO  
CUSTOMERS(based on claims determined as of Filing Date in the  
manner provided in the Act of 1970)

Request No. 22

Date May 17, 1974

Debtor      Morgan, Kennedy & Co., Inc.  
             Eugene L. Bondy, Jr., As TrusteeAddress     Rogers & Wells  
             200 Park Avenue, New York, N.Y. 10017

Mailing address for funds requested \_\_\_\_\_

(Check will be made payable to the Trustee for the debtor.)

Note: Before making payments to customers from SIPC  
advances, the Trustee must obtain court authoriza-  
tion.

Number of attached

pages:

1

(SIPC Form 11-1)

Advance requested for:

Credit balances      \$133,051.15

Cash in lieu of  
securitiesTotal                      \$133,051.15This request for advance is appropriate and necessary as  
provided for by the Securities Investor Protection Act of  
1970./s/ EUGENE L. BONDY, JR.      5/17/74  
Signature—Trustee              Date/s/ ROBERT S. KARMEL      5/17/74  
Signature—Attorney              Date







*Application of Eugene L. Bondy, Jr.*

## EXHIBIT I

SECURITIES INVESTOR PROTECTION CORPORATION  
 900 SEVENTEENTH STREET, N.W., SUITE 800  
 WASHINGTON, D.C. 20006 (202) 233-8400

June 28, 1974

Roberta S. Karmel, Esquire  
 Rogers & Wells  
 200 Park Avenue  
 New York, New York 10017

Re: Morgan Kennedy & Co., Inc.

Dear Roberta:

Mike Don informs me that the claim filed by the Trustees for Reading Body Works, Inc., Profit Sharing Plan Trust in the amount of \$133,051.15 is not now approved for payment. Therefore, I am returning Request No. 22 dated May 17, 1974 requesting funds in the amount of \$133,051.15, submitted per your letter of May 22.

In the last paragraph of your letter you ask us to forward \$20,000.00 in the event that the entire \$133,051.15 is not approved. I understand that a separate court order would be necessary before the \$20,000.00 can be advanced.

Please resubmitt request when the amount to be paid has been determined and approved.

Thank you for your cooperation.

Sincerely,

/s/ TOM

Thomas R. Cassella  
 Manager—Operations

*Application of Charles M. Solomon*

(Caption omitted in printing)

**Application for Order to Designate Claim of Trustees  
of Reading Body Works, Inc. Profit Sharing Plan**

COMMONWEALTH OF PENNSYLVANIA

COUNTY OF PHILADELPHIA ss:

CHARLES M. SOLOMON, being duly sworn according to law,  
deposes and says:

1. He has read the sworn application of Eugene L. Bondy, Jr. executed September 5, 1974, and adopts herein paragraphs from that sworn application numbered 1, 4, 5, 6, 8, 9, 10, 12, 13, 14, 15, 16, 17, 18, 19 and 20.

2. This application is being made for an Order (the form of which is annexed hereto) as follows:

(a) The claim of the Trustees of Reading Body Works, Inc. Profit Sharing Plan shall be deemed to be a cash claim in the amount of \$59,598.18, and a claim for securities in the amount of \$74,1336.25; and

(b) SIPC be ordered to pay to the Trustees immediately the sum of \$50,000.00 whether or not the interpretation of "customers" is or is not resolved at this hearing; and

(c) Each of the 108 beneficiaries of the Trust be deemed a separate customer and therefore the claim should be paid in full by SIPC; or

(d) Each of the three Trustees be deemed a separate customer and therefore the claim of the Trust should be paid in full as a cash claim of \$59,598.18 and as a claim for securities in the amount of \$74,336.25.

3. Paragraph 7 of the Bondy application is revised herein to aver that during the months of December, 1972 and January and February of 1973, the Trustees authorized the Debtor to execute the sales of certain securities

*Application of Charles M. Solomon*

on behalf of the Trust. These securities were delivered to the Debtor with powers signed by the Trustees in order to complete these sales. Some of the sales were completed and credited to the Trustees' account by the Debtor. See Exhibit A attached hereto and made part hereof.

Other sales were not completed because the Debtor gave the securities with powers attached to Chemical Bank and before March 9, 1973, the filing date of this liquidation proceeding, these securities had been seized by Chemical Bank as collateral for the indebtedness from the Debtor to Chemical Bank. See Exhibit B attached hereto and made part hereof.

Although these sales were never completed, the net proceeds were credited to the account of the Trustees by the Debtor. Efforts by the Trustees to recover securities held by Chemical Bank have resulted in litigation in the United States District Court of the Eastern District of Pennsylvania and that litigation is presently pending.

4. Paragraph 11 of the Bondy application is revised herein to aver that by letter dated June 26, 1973, counsel for the Trustees made formal claim upon the Debtor on behalf of each of the beneficiaries of the Trust. The claim (a copy of which was annexed to the Bondy application as Exhibit B) dated June 20, 1973, made claim in the alternative for money balances of \$133,236.15 and for securities as described in the attachment thereto (a copy of which was annexed to the Bondy application as Exhibit C). The footnote in the Bondy application in paragraph 11 is adopted.

Dated: Philadelphia, Pennsylvania  
October 14, 1974

/s/ CHARLES M. SOLOMON  
Charles M. Solomon

(Subscription omitted in printing)



## Application of Charles M. Solomon

## EXHIBIT "A"

Trade Date	Settlement Date	Present Location	Description	Net Proceeds
12/29/72	1/ 8/73	Sold	100 Syntex Corp.	\$ 8,234.83
1/31/73	3/ 2/73	Redeemed	\$50,000 Treasury Bill	50,000.00
2/13/73	2/21/73	Sold	200 Commercial Bancorp.	<u>1,363.35</u>
			Total cash claim	\$59,598.18

Trade Date	Settlement Date	Present Location	Description	Net Proceeds	Gross Proceeds
2/ 8/73	2/16/73	CB	300 Anaconda Co.	\$ 6,351.82	\$ 6,450.00
2/13/73	2/21/73	Sold By CB	300 Commercial Bancorp.	2,049.90	2,100.00
2/13/73	2/21/73	CB	100 Itek	4,333.31	4,400.00
2/13/73	2/21/73	CB	900 Pac. Tel & Tel.	15,821.88	16,087.50
2/13/73	2/21/73	CB	400 ATT \$4 conv., pfd.	24,097.41	24,350.00
2/13/73	2/21/73	CB	\$10,000 ATT 7% deb. Int. to 2/21/73	9,627.92	9,666.25 11.67
2/13/73	2/21/73	CB	\$10,000 ATT 8.75% deb. Int. to 2/21/73	11,170.83	11,037.50 <u>233.33</u>
			Total securities claim, excluding deductions for commissions and taxes		\$74,336.25

## Application of Charles M. Solomon

## EXHIBIT "B"

*Transcript of Hearing*

[2]

**Transcript of Hearing**

## A P P E A R A N C E S :

ROGERS &amp; WELLS, ESQS.

*Attorneys for the Trustee*

200 Park Avenue

New York, New York

By: MS. ROBERTA KARMEL, *Of Counsel*

FOX, ROTHSCHILD, O'BRIEN &amp; FRANKEL, ESQS.

*Attorneys for Reading Body Works Trust*

1401 Walnut Street

Philadelphia, Pennsylvania 19102

By: MICHAEL E. DON, Esq., *Of Counsel*

THE SECURITIES INVESTORS PROTECTION CORPORATION

By: MICHAEL E. DON, Esq., *Of Counsel*

MS. KARMEL: Your Honor, before we start I would like to introduce to the Court and ask for the admission for purposes of arguing this motion here today Mr. Charles M. Solomon, who represents the trustees for the Reading Body Work.

THE REFEREE: Yes. You are from Fox, Rothschild, et cetera?

[3] MR. SOLOMON: Yes.

THE REFEREE: And you are?

MR. McNAMARA: John McNamara, an associate of Mr. Solomon's of Fox, Rothschild.

THE REFEREE: I take it you are not admitted in the Southern District?

MR. SOLOMON: I am not.

THE REFEREE: You are admitted in Philadelphia?

MR. SOLOMON: I am admitted in the Eastern District.

THE REFEREE: I will admit you pro hac vice. I take it, basically, the question is a legal one?

*Transcript of Hearing*

MS. KARMEL: Yes, Your Honor, or let me say that the question raised by the trustee's application is purely a legal question and I am prepared to argue that question today.

Some of the questions raised by the application of the claimant, the trustees for the Reading Body Works, do involve a determination as to certain factual issues, some of which are presently contained in the trustee's [4] application and the cross-application of the trust, others of which I don't believe are really in dispute and could be provided in a further affidavit by the trustee or Mr. Raguson.

However, it is the trustee's position that if the trustee's application is granted, these issues will all become moot. So, we would suggest that the Court not address itself to these further issues until it decides the trustee's application.

THE REFEREE: Where is the dispute on the application?

MS. KARMEL: The dispute on the application is with SIPC.

THE REFEREE: Only with SIPC? You and the trust are on common ground?

MS. KARMEL: Not entirely. I think the trust will be happy if the trustee's application is granted. If the trustee's application is denied, then the trust has further other points to bring up.

THE REFEREE: The first thing, logically, will be for me to hear the trustee's [5] position and to ask SIPC if it has any opposition or papers.

MR. DON: They were filed quite a while ago.

THE REFEREE: What do they consist of?

MR. DON: A memo of law.

THE REFEREE: Exclusively a memo of law?

MR. DON: Yes. I didn't think the proper procedure would be to file a cross-motion or motion to dismiss, or anything like that. We felt it would be appropriate to oppose.



*Transcript of Hearing*

THE REFEREE: On the record, I have two parties on the same side and you opposing without anything except a policy position. Let us see if we can't find your memo.

MR. DON: I can supply a copy right now.

THE REFEREE: We are under a state of continuous flux here. I hope I have finally landed the right people to help me.

Let us treat, Mr. Rayvid, on the record the memo of law interposed by the Securities [6] Investors Protection Corporation as the guardian administrators of this act their memo of law as, basically, opposition to the legal position advanced by the trustee vis a vis this trust so that at least we have a record in case SIPC is aggrieved and they will have standing to go up. Otherwise, we just sit here.

MR. DON: Thank you.

THE REFEREE: Now then, Ms. Karmel, let me hear what you must tell me?

MS. KARMEL: Your Honor, the trustee's application is an application to ask that the claim filed by the three trustees of the Reading Body Works, Inc. profit sharing plan trust——

THE REFEREE: Is that a single trust?

MS. KARMEL: Which is a single trust, will be designated as the individual claims of one hundred eight persons who were the beneficiaries of the trust on the filing date of this proceeding.

THE REFEREE: All right.

MS. KARMEL: The trustee has also applied for an interim advance of twenty thousand [7] dollars to the trust pending a final decision on the trustee's entire application. I have been advised that SIPC would not object to this, and I would hope we could at least get this twenty thousand dollars to the trust promptly.

THE REFEREE: Give me an order on SIPC's consent. I am sure the trust is good for it if something is ever reversed.

MR. DON: Yes.

*Transcript of Hearing*

THE REFEREE: Give me an order granting on consent of SIPC so much of your notice of application as sought an interim advance.

Ms. KARMEL: There is a proposed order attached to our papers.

THE REFEREE: I like separate orders because these motions I will want for a decision.

MR. DON: Well, Your Honor, I have some minor problems with the language of that order, anyway.

THE REFEREE: In that case, Ms. Karmel, why don't you draft an order providing for the granting of the relief but with the sub- [8] joined consent as to form and substance.

Ms. KARMEL: Fine. Your Honor, if I may, I would like to point out that certain matters upon which the trustee's application is based are not in dispute by anybody. First of all, the trust is a profit-sharing plan of the Reading Body Works, Inc. and there were one hundred eight employee-beneficiaries on the filing date.

The books and records of Morgan Kennedy reflect that there were sales of various securities for the account of the trust prior to the filing date and that as at the filing date there was a free credit balance in the amount of one hundred thirty-three thousand fifty-one dollars and fifteen cents.

THE REFEREE: That's with the reduction of one hundred eighty-five dollars which you mentioned?

Ms. KARMEL: Exactly. The trust is claiming a total of this amount of money. There is a dispute which, as I said, we would prefer the Court to defer.

THE REFEREE: As to the dollars?

[9] Ms. KARMEL: Not as to the dollars, as to whether this should be treated as a cash claim or a claim for cash and securities, and I say that is part of the cross-application by the trust which we would have to submit some further facts on.

But, it is the position of the trustee that this is a cash claim.



*Transcript of Hearing*

THE REFEREE: I don't understand SIPC's position.

MR. DON: As to what, Your Honor? We agree with the trustee that this is a cash claim.

THE REFEREE: No, as to the first part. I am just reading ahead. I take it you are taking the position like an indenture trustee is a single beneficiary?

MR. DON: The trust is a single customer, yes, Your Honor.

THE REFEREE: I have held akin to that in a different context. I doubt very much this is the kind of context that the statute demands.

MR. DON: Your Honor, to be quite frank [10] with you, I think it is not only commanded by the statute, but I don't see anything in the statute or in the legislative history to indicate otherwise.

THE REFEREE: If I have a trustee in bankruptcy, who deposits all his funds at Banker's Trust across the street and there are twenty-five separate bankruptcy estates of which he is the trustee, for purposes of federal deposit insurance is he a single customer?

MR. DON: I believe there would then be twenty-five separate insured deposits.

THE REFEREE: You are not impressed if I apply that kind of rationale here?

MR. DON: The reason for that is based upon the regulations given the FDIC by the statute—we have no regulation or authority—

THE REFEREE: So, you are saying if I don't have a clear command of the statute as to this, it must be that Congress decided not to let me do this?

MR. DON: It's more than that, it's that the statute clearly defines customer one [11] way whereas the FDIC doesn't.

THE REFEREE: Okay.

MS. KARMEL: Your Honor, this is our position and I would like to go through it step by step. First of all, the primary purpose of the 1970 act was to bolster investor

*Transcript of Hearing*

confidence in the financial stability of the securities industry and, in fact, Congress was attempting to protect the small individual investor from losing securities and monies that were entrusted to his broker-dealer.

THE REFEREE: The answer to that is the small investors put all their trust in big daddy and big daddy is one person?

MS. KARMEL: That is correct. For this purpose insurance coverage for broker accounts was provided. Section 6F(1) which is what really must be interpreted here, does not provide for insurance coverage of accounts, it provides for the payment and satisfaction of the claims of customers. SIPC has taken the position in its brief, which unfortunately I haven't had a chance to see yet, but on Pages 3 to 5 of SIPC's brief, SIPC takes the [12] position that the Court must find if each of those welders, grinders, linemen and other employees of the Reading Body Works had a separate account with the debtor for the trustee's application to be granted, obviously you are reading "customer" to be someone who has an individual account in his own name and did business for himself.

MR. DON: Yes.

MS. KARMEL: The 1970 Act defines a customer in Section 6A(2) as a person, not an account, but as a person who has a claim because of certain types of security transactions and an account is merely a record which a broker-dealer keeps of transactions by a customer, and I would contend that SIPC is confusing a paper record of debits and credits for the people whose claims the trustee is trying to satisfy.

Now, as this Court knows from this and other cases, the 1970 Act is not as clear as any of us would like on a number of matters, and we believe this is one. There is a definition of customer in the statute and it's that [13] definition that we are trying to grapple with here.

I think it is relevant and it is our position that the legislative history shows that Congress hoped the Act's cover-

*Transcript of Hearing*

age would be comparable to the coverage to bank depositories under the FDIC.

THE REFEREE: I think the politicians who enacted this act would be chagrin to find their constituents would be thrown out of the box.

MS. KARMEL: Yes, we believe that. It is our contention that under the FDIC this claim would be treated as one hundred eight depositors. SIPC takes the position that the result is reached by way of the rulemaking powers of the FDIC and SIPC states it has no such rulemaking authority.

THE REFEREE: And I should not, therefore, read something in?

MS. KARMEL: The position of the trustee is that if SIPC does not have the rulemaking authority it is for the Court—

THE REFEREE: I am not making rules. [14] I think we are using rules differently. What he means, Mr. Don—I think what he is saying is that rules duly promulgated pursuant to a statutory grant have the force of law.

MS. KARMEL: Yes.

THE REFEREE: Absent such rules indicating that those charged with the administration of this statute, to wit, the Securities Investors Protection Corporation, absent such rules they are charged with administering the act and construing the act in the absence of some guiding rules because if there were light to be shed on this by rules, there would be such rules.

Your answer is, I suppose, that rules and regulations of the typical understanding merely implement the bare bones of the statute?

MS. KARMEL: Yes.

THE REFEREE: But, the construction of the words that Congress wrote is for me, in any event, regardless of what they may or may not have said?

MS. KARMEL: That's right. We contend further that the legislative history does [15] demonstrate a notion on the

*Transcript of Hearing*

part of Congress that the statute could be interpreted to provide coverage comparable to that of the FDIC and, therefore, in interpreting the word "customer," the way in which the FDIC has defined depositor, would be persuasive.

THE REFEREE: I think, frankly, the best index of what the statute could be interpreted to be would be what Congress had in mind. What I am sure of is that what Congress had in mind was the average small investor. When you deal with people like this, my friend, in a laboring blue collar craft, and placing all their wherewithal with big daddy—let me ask this of the fund—

What is the physical means that you had on your books? Supposing one of your persons should die or become eligible, how do you deal with him?

MR. SOLOMON: I am not sure I can answer the administrative problem.

THE REFEREE: I want to know to what extent you kept these people separate?

MR. SOLOMON: We had separate accounts [16] and these became vested funds for each of the beneficiaries. Our trustees could produce that.

THE REFEREE: You would render statements from time to time indicating that some of their positions had either weakened or strengthened?

MR. SOLOMON: I don't think they ever weakened. I think by law each year we are required to notify the beneficiaries of what their balances are.

THE REFEREE: If he dies or becomes eligible as of a certain time, that is?

MR. SOLOMON: That's right.

THE REFEREE: He is not a common tenant in a given pot?

MR. SOLOMON: He is given a dollar amount as of a given time.

THE REFEREE: Are all the accounts equal?

MR. SOLOMON: No.



*Transcript of Hearing*

THE REFEREE: Depending upon the number of years?

MR. SOLOMON: Percentage in years.

[17] MS. KARMEL: If you feel it would be helpful, the trustee for the trust did provide my trustee at some point with a list of the one hundred eight beneficiaries and their exact percentage interest. We could submit that to the Court if you think that is important.

THE REFEREE: I don't think Mr. Don is going to quarrel with the physical way the trust stands. Is there any law or decision construing a comparable type situation? I had a case recently in which an indenture trustee represented the beneficiaries of the indenture. He had done very well for that group in a Chapter XI in making certain that the debtor, in offering a plan to his creditors under Chapter XI, made provision for the beneficiaries of the trust and he, succeeding in this, then made an application to the Court—let me start at the beginning.

The indenture trustee in wishing to take an active part in these proceedings tried to vote in connection with the official elections in the course of the bankruptcy the claims of each of the beneficiaries of the trust con- [18] tending well, we have one thousand beneficiaries here, I control this thing. I disallowed it on the grounds that there was but one single creditor involved here, the indenture trustee.

Now, I know there are texts on indentures and I am sure there must be comparable situations in which the beneficiary of the trust were separate, each into his own. You might want to examine that. Is that covered here?

MS. KARMEL: No, Your Honor, it isn't. Actually, there are cases under the Securities & Exchange Act of 1934 which, I think, are relevant in the sense that Section 2 of the 1970 act says SIPC should be interpreted or should be viewed as a amendment to the 1934 act.

There are cases under the 1934 act in which the beneficiaries of a trust have been permitted to sue under Section

*Transcript of Hearing*

10B and Rule 10B(5) as separate entities. I believe those cases are relevant, really, because they are cases under the Exchange Act.

I think the Exchange Act is the relevant [19] statute here and I would point out that the Exchange Act and SIPC are remedial pieces of legislation and we believe they should be given a liberal construction in a case like this to protect those persons such as the beneficiaries of the trust that this statute was enacted to protect.

SIPC has criticized the position of the trustee as being based on a general vague concept of equity. We naturally admit here that the trustee is trying to do equity as we would hope this Court is trying to do equity.

THE REFEREE: If I am guided in construing ambiguous or silent legislation and if I am told by you, Mr. Don, that the position you want me to take here is probably at odds with what Congress really had in mind, if it had anything in mind as Justice Holmes used to say, I would apply broad equitable principles in striving for a construction of a statute which comports with what Congress really would have done if it knew what it was doing. I know you will give me a competing canon of construction.

[20] Ms. Karmel is right, there are equitable principles that dominate, if not control this Court's bankruptcy jurisdiction.

MS. KARMEL: I would like to point out, Your Honor, two factors which, again, really go to the equities of the situation. One is that not only were the beneficiaries of this trust the very kind of small investors Congress was trying to protect, but Congress was trying to protect them in this kind of situation because in the course of the trustee's examination of various witness, there are admissions that a fifty thousand dollar treasury bill which is part of the monies being claimed here was illegally converted by this debtor and others.

These, as shown in the papers annexed to the cross-application of the trust, and according to the books and

*Transcript of Hearing*

records of Morgan Kennedy, these securities were sold well before the date of bankruptcy and it's only because this debtor was playing so fast and loose with the property of customers that there was even one hundred thirty-three thousand dollars [21] to be claimed as of the filing date here.

This money should have been paid to the trust long before the filing date and, again I say, I think this is just the kind of situation that Congress had in mind.

THE REFEREE: Why didn't they do it, it would have been easy.

MS. KARMEL: They weren't acting in a proper fashion.

THE REFEREE: Congress?

MS. KARMEL: Morgan Kennedy.

THE REFEREE: Why didn't Congress? If Congress saw fit to cover so many people, why didn't they do it? They did it in the Federal Deposit Insurance Corporation.

MS. KARMEL: There is no difference here. It's implementing the rules of the FDIC.

THE REFEREE: Did you want to add something, Mr. Solomon?

MR. SOLOMON: I would like to state my position when Ms. Karmel is through because I am in substantial agreement with her.

THE REFEREE: I am not surprised.

[22] MS. KARMEL: I would like to state this is the only claim filed in this proceeding that is beyond the bounds of SIPC limitations to fifty thousand dollars or twenty thousand dollars. If this claim is paid then all of the claims in this liquidation which have been filed and which the trustee did not contest as being proper or invalid, will have been paid.

Again, I think looking at this in an equitable fashion, that is something the Court may wish to take into consideration, although it does not relate to the merits of this claim.

*Transcript of Hearing*

THE REFEREE: The fact you paid other claims that SIPC didn't litigate doesn't mean I have to pay one where SIPC disputes.

MS. KARMEL: It's not like we had one hundred claims like it.

THE REFEREE: If you did I would assume with your typical candor you would have told the Court the weakness in SIPC's position. That I am not concerned with.

Anything else, Ms. Karmel, that you [23] would like to advance?

MS. KARMEL: No, Your Honor. We feel it's a question of interpreting the word "customer" in the statute and that the legislative history and principles of equity would dictate that the word "customer" be interpreted so that the one hundred eight beneficiaries will be paid the money that was due and owing on the filing date.

THE REFEREE: What you mean is that the money would be placed into the trust for the benefit of these beneficiaries as though they were all separate individuals?

MS. KARMEL: Yes.

THE REFEREE: What did you want to add?

MR. SOLOMON: We are in substantial agreement with Ms. Karmel, but I think since SIPC has taken the position there are not one hundred eight limitations to be applied but only one, I would like to state our position very briefly to the Court.

THE REFEREE: Please.

MR. SOLOMON: The only two points in which we have some disagreement with Ms. Karmel [24] are these:

In the first place, we think that this is not a totally cash claim, it's not a claim for cash alone. I understand why the trustee so interpreted it and that's because the broker has entered a credit in our account for one hundred thirty-five thousand dollars plus.

However, I say that this is a fiction because the thrust of the matter, as I said in my application under oath, is



*Transcript of Hearing*

that the major portion of the shares that we offered for sale and delivered for sale were never sold. These shares are still in the possession of Chemical Bank and we say that as long as our certificates are in the possession of Chemical Bank, this is not simply a claim for cash, it's a claim for securities. Therefore, we have itemized them in a memorandum of law, which I won't bother to repeat at this point.

THE REFEREE: Do I have it?

MR. SOLOMON: I would hope you have it, Your Honor. I sent it to you—let me summarize it for you. According to the computation we presented our claim for cash would be [25] for fifty-nine thousand five hundred ninety-eight dollars and eighteen cents and the value of the securities that are still in the hands of Chemical Bank never delivered for sale amount to seventy-four thousand three hundred thirty-six dollars and twenty-five cents.

THE REFEREE: You have a typo in Paragraph A.

MR. SOLOMON: I think we have too many dollars, yes.

THE REFEREE: Seventy-four thousand three hundred thirty-six dollars and twenty-five cents?

MR. SOLOMON: The correct figure is seventy-four thousand three hundred thirty-six dollars and twenty-five cents. Now, we have this difference which, I think, is a conclusion of fact based on the facts that are not denied that if the securities which we secured for sale were never delivered for sale and are still in the hands of Chemical Bank I don't see how the trustee can properly conclude that we are relegated to a cash claim which would limit us to twenty thousand dollars [26] per customer instead of fifty thousand dollars.

Therefore, I am submitting to Your Honor that we are making both a cash claim and a securities claim and we did that from the very beginning when we filed our claim with the liquidating trustee.

THE REFEREE: Now, is there a question of fact on that?

MR. SOLOMON: It's a conclusion of fact.

*Transcript of Hearing*

THE REFEREE: You don't conclude facts, you find facts and conclude legal principles. What facts do you want me to find?

MR. SOLOMON: I want you to find that our claim is based upon the non-delivery of securities in part and, therefore, it's a claim for securities which would give us a limit of fifty thousand dollars per customer, that we would not be confined to twenty-thousand dollars per customer.

Now, this is moot, Your Honor, if you are to decide that there are one hundred eight customers here and that would solve the problem and make my entire argument moot.

[27] THE REFEREE: Is that agreed, Ms. Karmel?

MS. KARMEI: Yes, and if Your Honor wishes, the trustee could submit papers and reply on this point.

THE REFEREE: Just give me something so I will make a complete record.

MR. SOLOMON: The second point and the real reason why I decided to appear here is because if Your Honor does not adopt the view of one hundred eight customers, I think that the opposing conclusion of SIPC that there is only one customer is dreadfully wrong and I would therefore propose that there is an alternative, a middle ground, three grounds.

THE REFEREE: Meaning the number of trustees of the trust?

MR. SOLOMON: That is correct. The reason I press the other point is because if there are three trustees who are customers then the cash claim for sixty thousand dollars minus would be allowed and the securities claimed for seventy-four thousand dollars [28] would also be allowed which would give us complete recovery. Now, the justice of our position, I think comes best out of the opinion of Mr. Don for SIPC wherein he says that the one hundred eight beneficiaries are not the customers, that the trustees are the customers.

*Transcript of Hearing*

THE REFEREE: I don't think the trustees are the customers. I think the trust is the customer. How I view the trust——

MR. SOLOMON: That's as fictional as anything else.

THE REFEREE: I would just as soon give the one hundred eight people than assume that three agents of the trust are customers.

MR. SOLOMON: I think the best ground is probably that which Ms. Karmel has advanced. I think Your Honor has a thorough grasp of the situation and I will conclude by pointing out that I will agree with Mr. Don that the word "customer" as defined in the Act is a very broad definition and the trustees who opened the account, dealt with the account, who delivered the securities, are certainly in the definition of "customer" and SIPC has no power [29] to alter that definition by any attempted rulemaking.

THE REFEREE: The fact is they haven't altered it.

MR. SOLOMON: Not effectively. Thank you, Your Honor.

THE REFEREE: You have a heavy burden, I think, Mr. Don. If I understand you, you have one hundred eight separate customers here, namely, the beneficiaries of the trust and they would assume what status under the Act?

MR. SOLOMON: They would be the customers.

THE REFEREE: How much would they get?

MR. SOLOMON: Twenty thousand dollars per each customer which would be more than adequate to cover them under the cash concept. In other words, even——

THE REFEREE: Some would be entitled to less, wouldn't they?

MR. SOLOMON: They would all get less because I don't think any individual claim exceeds twenty thousand dollars.

MS. KARMEL: We computed this at some [30] point. I believe there is one beneficiary whose claim is such that it would be just a shade under twenty thousand dollars.

THE REFEREE: In other words, if I rule there are one hundred eight beneficiaries here, one hundred eight sepa-



*Transcript of Hearing*

rate customers, what is the total amount that SIPC would have to pay?

MR. SOLOMON: The gross claim of one hundred thirty-three thousand dollars.

THE REFEREE: That's all there is in dispute here?

MR. SOLOMON: That's right, that's all there would be.

THE REFEREE: If I decide that the three agents of the trust are the customers so there are three of them, how are they covered, up to the one hundred thirty-three thousand dollars?

MR. SOLOMON: We would say there would be a full coverage.

THE REFEREE: Cash and securities?

MR. SOLOMON: That's right.

MS. KARMEL: I think we would say there [31] would be coverage in the amount of sixty thousand dollars because there is a cash claim.

THE REFEREE: Sixty thousand dollars plus seventy thousand dollars?

MS. KARMEL: No.

MR. SOLOMON: The liquidating trustee views this as a cash claim purely.

THE REFEREE: In that case you are limited to twenty thousand dollars a customer?

MR. SOLOMON: That's right. That would be sixty thousand dollars. I say—and this is the reason why—I say this is not simply a cash claim because most of our securities were never sold.

THE REFEREE: I get to that only if I rule there are not one hundred eight separate customers within the meaning of the legislation.

MR. SOLOMON: Precisely.

THE REFEREE: If I hold this to be a single customer, namely, the entity itself without regard to each beneficiary, that is to say, if I adopt Mr. Don's position, then they are covered for twenty thousand dollars and [32] that's the end of that, right?



*Transcript of Hearing*

MR. SOLOMON: If you also adopt this is only a cash claim, not a securities claim.

THE REFEREE: Will I need an issue of fact, testimony on the securities?

MS. KARMEL: Well, Your Honor, we will submit an affidavit and a memo of law on this point. I do not believe that Mr. Solomon will take issue with our affidavit. We have discussed the facts. If he does I suppose we may have to go to trial or he may have to submit another affidavit. Your might want to schedule some time when you want us to put these papers in.

THE REFEREE: I will. If I adopt the ground that we have three customers, the agents of the trust, you would concede he is entitled to sixty thousand dollars?

MS. KARMEL: Yes.

THE REFEREE: How do I reach the other question? Just on the papers you would submit to give them the securities position for the seventy-three thousand dollars?

MS. KARMEL: The problem with this, you [33] see, if this really, probably, would have come before the Court on an objection by the trustee to the claim submitted here. This has always been anticipated by way of the cross-application filed by the trust.

But, if the trust does not dispute whatever affidavit as to the facts then I suppose you could decide this very much like a summary judgment motion.

THE REFEREE: So, I would need an affidavit as to the facts as alleged by you and, I suppose, the books and records of the company.

MS. KARMEL: We would be relying on the books and records of the company.

THE REFEREE: There would be no contest as to what those books show and then I would be asked to rule that on the facts undisputed alleged by the affidavit, I would then have to decide a second question, namely, have they got a securities position, right?

MS. KARMEL: Yes.

*Transcript of Hearing*

THE REFEREE: That's if I adopt the view that we are dealing only with three cus- [34] tomers or one customer. Now, Mr. Don, you have something of a burden.

MR. DON: I will try to bear it, Your Honor. I guess first of all I should talk about the intent of Congress.

THE REFEREE: How do you know what it is?

MR. DON: I don't myself because I was not there, although our general counsel was there. He was chief counsel on the house sub-committee which drafted this legislation.

I think it should be noted that the house committee that drafted the legislation was the House Banking & Commerce Committee. This is the same committee that deals with FDIC legislation. It knew very well what the FDIC rules provide, yet it did not provide the same rulemaking power to SIPC for some reason.

I think that, at least, has some bearing on the intent of Congress.

THE REFEREE: If they intended anything.

MR. DON: The FDIC's rules and interpretation of its own rules are set forth in twelve CFR, Section 30.101, I believe, Your [35] Honor. In any case, they have provided in their interpretation that where the trust in question is an irrevocable trust under State law the beneficiaries of the trust will each be treated as separate depositors and each separately insured.

They further provide if the trust is an irrevocable trust under applicable State law, that there should be one customer, the trust. I don't see how our statute, the 1970 Act, could be interpreted one way or the other. If you interpret—if you say the beneficiaries are customers, you ignore the question whether there is a difference under our statute between a revocable trust and an irrevocable trust. SIPC has no power to regulate this question.

To say that you are going to open up a hole in the statute like this so that you could have completely differ-

*Transcript of Hearing*

ent treatment than the FDIC, and nobody with authority to promulgate the rules as to what type of trusts are covered and what type are not—

THE REFEREE: It's the Court's feelings. [36] Courts don't create gaps in legislation, they fill in the intestacies. What happened here was Congress rendered ambiguous legislation. They did not charge the administrative agency charged with its performance; they didn't give them power to implement the statute. So, it kind of left it to the Court.

MR. DON: That would be true if the 1970 Act did not provide a complete and exhaustive definition of the term "customer." The Federal Deposit Insurance Act does not provide any definition at all of the term "depositor," and it provides a very vague definition of "deposit" which means basically anything which is put into an account in the bank without reference to who put it in there.

It has left it entirely up to the rules adopted by the FDIC to fill that gap. In our statute it has who is a customer and it says a person with a claim on account of securities for various reasons or a claim for cash deposited for the purchase of securities.

Now, I don't think Your Honor—

[37] THE REFEREE: Can a trust be a person?

MR. DON: Yes, Your Honor.

THE REFEREE: A trust can be a person?

MR. DON: A trust is a person in this case.

THE REFEREE: And its trustees are not?

MR. DON: That's right. Can you imagine a situation with two trusts, each with a claim for one hundred thousand dollars and one trust had one trustee and got twenty thousand dollars and another trust had five trustees and, therefore, got one hundred thousand dollars?

THE REFEREE: Think how much wiser it would be to count the beneficiaries and not be moved by the number of trustees.



*Transcript of Hearing*

MR. DON: I think it would be wiser to count the beneficiaries than the number of trustees. But, the wiser thing would be to count the number of trusts. The fact is the beneficiaries of these trusts have no right to the funds in the trust other than under the terms of the trust. They have vested rights that they may not be able to realize for twenty [38] or thirty years. I don't know how it works.

How can it be said they are customers with claims for securities in accounts that the trust held at Morgan Kennedy? They have no right to the funds.

THE REFEREE: It's not the most sympathetic position ever advanced by SIPC.

MR. DON: I am quite willing to admit it's not a sympathetic position. I think the statute is so clear and the legislative history that any attempt to adopt the FDIC type of protection—

THE REFEREE: You watch me.

MR. DON: I will, Your Honor, with interest.

THE REFEREE: This statute is ambiguous. Obviously, the statute did not contemplate a controversy of this kind involving a fact pattern of his kind. It's not astounding that Congress can't touch every base.

MR. DON: Except, you are dealing with a committee which was thoroughly familiar with what was done with the FDIC.

THE REFEREE: You are imputing something [39] more than most judges are willing to impute. That is a committee which is frequently not made of lawyers, although probably most have the knowledge, sophistication and understanding to integrate what was done in some legislation thirty years ago with what they are doing today—

MR. DON: I believe officers of the Federal Deposit Insurance Corporation testified at the hearings on this legislation.

THE REFEREE: I doubt very much that Congress thought of this. What you are asking me to do is take the plain language of the statute. You say it has plain meaning, you



*Transcript of Hearing*

say it expressed the limit to which Congress was willing to go, that's the end of it and the Court then has no power to interpret it.

MR. DON: I guess what I am saying, Your Honor, is that you have ample authority to interpret but an interpretation implies staying within the bounds of the statute.

THE REFEREE: You say it says what it says, that's all it says, and I can't add or detract?

[40] MR. DON: I think it would be stretching the statute to the breaking point to say that the beneficiaries were intended to be covered.

THE REFEREE: It might be stretching it to its breaking point, but in the absence of some exclusion by Congress for this type of situation, don't I look to what Congress had in mind, how to help the small investor?

MR. DON: The investor is the trust.

THE REFEREE: You have a tough road to hoe, quite frankly. I don't think you would think me prejudging the case if I told you that I feel if the Court had a way in which it could find here as the trustee suggests I will. This is your trustee, remember.

MR. DON: If I were in your shoes, if I could find a way——

THE REFEREE: You can have the job now.

MR. DON: I couldn't find a way.

THE REFEREE: Let me say this to you, also. This is a rather ambiguous relationship that exists here. I agree with you that [41] in analogizing this to an administrative agency type setup you are the agency charged with the administration of the statute and your interpretation and the matter of first impression would be entitled to considerable weight. But, this is not that kind of case where an attorney for the Department of Justice speaking, for example, for the immigration service comes into court and states an administrative policy decision by the Commissioner and the Commissioner's policy decision is trans-

*Transcript of Hearing*

lated down the line to the lowest rung of his workers in any district office.

You, the administrators, have designated a trustee. You have put a great deal of confidence in his and his legal staff's acumen and understanding so that your view is not entitled to the automatic great weight which I would give to any administrative agency charged with administering an act. You delegated an enormous amount of responsibility to your trustee here and your trustee read the statute and diametrically is opposed to you as a policy matter.

[42] MR. DON: May I speak for one more minute?

THE REFEREE: Yes.

MR. DON: As to that last point, of course you know we have absolutely no control over our trustees once we have designated them. They are officers of the Court and subject to Your Honor.

THE REFEREE: I'm glad.

MR. DON: The other point is as to our administrative expertise. We have adopted rules. We do not contend that the rules are binding on a Court.

THE REFEREE: They don't have the force of law under Ricardiv Shaunessey.

MR. DON: Their internal policy decision states very specifically what is supposed to happen when a trust is a customer.

THE REFEREE: Do you have a copy of that policy decision?

MR. DON: Yes.

THE REFEREE: Who was it transmitted to? When the Attorney General makes a policy decision he transfers it to his subordinates. [43] This trustee is not your subordinate, he is merely a gratuitous agent.

Let's understand something. SIPC is not eminently disinterested in what I do because SIPC to the extent that it has got to make payments has a pecuniary interest in the way I go. It's unlike a different kind of situation.

*Transcript of Hearing*

So, you could make your own guidelines down the line. They are still colored with what your interests in these proceedings are.

MS. KARMEL: I do think it should be noted these rules were adopted in October 1971 a long time before this issue ever arose.

THE REFEREE: I haven't seen one in Weis. I don't think my colleagues have seen one in Baroff or Salmon. I don't think the issue has come up.

MR. DON: It has not come up.

THE REFEREE: The fact you came out with this three years ago and the issue never arose doesn't mean anything.

MR. DON: The rules make it clear that the trust is the customer and not the beneficiary. [44] arises.

MS. KARMEL: I don't think these rules are determinative of the issue here. The rules are discussed in both the briefs of the trustee and SIPC. There is no rule specifically covering this issue.

THE REFEREE: Could I now have that memo of law, Mr. Don?

MR. DON: Yes.

THE REFEREE: Which you promised me and for which I apologize for not having the original. I will treat it as a paper of SIPC in opposition to the position expressed by the trustee.

MR. SOLOMON: Did Your Honor get a copy of our memo?

THE REFEREE: I did see this brief. This is the one where you annexed a copy of my colleague, Herzog's decision. I don't see what it has to do with this except for the reliance he placed on your internal rules.

MR. DON: Yes.

THE REFEREE: I have my own feelings. I spent ten years dealing with administrative [45] law and administrative policies. This is not entitled to that great weight.

MR. SOLOMON: Did you get our memorandum?

*Transcript of Hearing*

THE REFEREE: I don't know. If I did, I will have another one. If I didn't, I will enjoy this. I will reserve decision. Let me give Ms. Karmel and you people a timetable wherein Ms. Karmel can give me undisputed facts concerning the securities aspect of these claim.

Supposing, Mr. Rayvid, you will try to get the minutes to Ms. Karmel by the 15th of November and I will take an affidavit from you by the 29th of November and anything else. Do I need another memo of law?

MS. KARMEL: We will submit a memo of law on the point that supports the trustee's view this is a claim for cash.

MR. DON: We would agree with the trustee.

THE REFEREE: There will be no dispute there?

MR. SOLOMON: We dispute that, Your [46] Honor.

THE REFEREE: Ms. Karmel will give me an affidavit and memo of law in which she will argue if I go other than the one hundred eight beneficiaries, that these are cash customers, and that ends it, by the 29th. You may reply by December 9th on your point that you are entitled to securities and cash.

MR. SOLOMON: Thank you.

THE REFEREE: Does that state it fairly well? Is there any rush on this?

MS. KARMEL: Well, the claim has been pending a long time.

MR. SOLOMON: Nineteen months, Your Honor. It's supposed to be paid promptly.

THE REFEREE: I will shorten the time.

MS. KARMEL: I would rather not have the affidavit due before November 29th. Possibly we can do this by stipulation. I would like to be able to send the affidavit to you before I submit it.

MR. SOLOMON: I don't think there is a dispute.

MS. KARMEL: I don't think so, either. [46a] I would like you to give us the time to have that kind of records before the Court.

THE REFEREE: I will reserve decision as of the 29th. Thank you, ail.



*Memorandum Opinion of Bankruptcy Judge Babitt*

(Caption omitted in printing)

**Memorandum Opinion**ROY BABITT, *Bankruptcy Judge*:

Eugene V. Bondy, Jr., as trustee for the liquidation of the stock brokerage business of Morgan, Kennedy & Co., Inc. has petitioned this court for an order declaring that the single claim filed by the Trustee of the Reading Body Works, Inc., Profit Sharing Plan Trust for \$133,051.15 be considered for distribution purposes as separate claims of the 108 beneficiaries of that profit-sharing trust and that, therefore, the liquidating trustee pay this claim in full under the scheme of the relevant statute. Morgan, Kennedy is presently in liquidation under the statutory scheme provided by the Securities Investor Protection Act of 1970, 15 U.S.C. §§ 78aaa, et seq. (SIPA).

The following undisputed facts set the stage for the controversy:

Pursuant to the terms of a profit-sharing plan adopted in 1957, Reading Body Works, Inc. (the "Company") established its trust for the benefit of its employees. The trust fund was administered by independent trustees and was maintained by yearly contributions made by the Company based upon its net earnings. Employees accumulated percentage interests in the fund based on their annual compensation level and consecutive years of service. Separate "accounts" were maintained for each employee in which he had a non-forfeitable vested interest subject to certain conditions pitched to termination of employment with the Company. Credit entries were made to each "account" according to the employee's proportionate share of the Company's yearly contribution and any increase in the market value of the fund.

On March 13, 1973, it was determined that the customers of Morgan Kennedy were in need of the protection

*Memorandum Opinion of Bankruptcy Judge Babitt*

afforded by the 1970 "SIPA" and Eugene L. Bondy, Jr. became the trustee for the liquidation of Morgan Kennedy's business. In accordance with the scheme of that statute, a claim by the profit-sharing trust was filed in the sum of \$133,501.15,\* the amount owed by Morgan Kennedy to the Trust on the relevant date of the proceedings to liquidate.

By letter dated October 9, 1973, Morgan Kennedy's trustee informed the Corporation created by SIPA to administer the Act (SIPC), 15 U.S.C. § 78ccc, that he intended to treat each of the 108 beneficiaries of the profit-sharing trust as a separate "customer" for purposes of the recovery limit provided in Section 6(f) of the SIPA, 15 U.S.C. §§ 78fff(f)(1). He, therefore, requested that SIPC advance the full amount of the claims of the individual beneficiaries.

SIPC, however, informed Morgan Kennedy's trustee by letters dated May 23, 1974 and June 10, 1974 that it did not consider each beneficiary as a separate "customer" but felt that the profit-sharing trust itself was a single entity "customer" within the meaning of SIPA. From this SIPC concluded that it would therefore advance only a maximum of \$20,000 as called for by the SIPA.

The issue thus presented is whether each of the 108 beneficiaries is a separate "customer" within the meaning of Section 6(f) of the SIPA, 15 U.S.C. §§ 78fff(f)(1). After carefully considering the legislative policy behind the creation of the SIPA it is my conclusion that the purpose of the Act is satisfied by treating each beneficiary of the trust as a separate "customer" and therefore entitled to the full coverage afforded.<sup>1</sup>

\* The amount and validity of this claim as a claim is not contested in this proceeding. What is in controversy is the reach of the estate's exposure because of the nature of the trust and its beneficiaries.

<sup>1</sup> Since I have concluded that each of the 108 beneficiaries is a "customer" within the meaning of the SIPA there is no need to reach the alternative argu-

*Memorandum Opinion of Bankruptcy Judge Babitt*

The SIPA and SIPC were created by Congress to provide investors with insurance against the loss of securities and cash left broker-dealers who thereafter encounter severe financial difficulties and must be liquidated. *U. S. Code Congressional and Administrative News*, 91st Cong., 2d Sess. 1970, p. 5255. Accordingly, the SIPA provides that the SIPC:

"... shall advance to the trustees such moneys as may be required to pay or otherwise satisfy claims in full of each customer, but not to exceed \$50,000 for such customer. . . ." Section 6(f)(1), 15 U.S.C. § 78fff(f)(1) [emphasis added].<sup>2</sup>

This controversy thus turns on the construction of the word "customer." The Act defines "customers" as:

"... persons (including persons with whom the debtor deals as principal or agent) who have claims on account of securities received, acquired, or held by the debtor from or for the account of such persons. . . ."

Since Congress, in enacting the SIPA, meant to protect innocent investors, I have no doubt that the word "customer" should be read to include the individual beneficiaries of the profit-sharing trust. In effect, each beneficiary maintained his own account with Morgan Kennedy and it is quite irrelevant that books of this stockbroker carried the trust entity as the "owner" of the account or, for its own bookkeeping purposes, as its customer.

The Series 100 Rules adopted by the SIPC to provide guidelines for identifying accounts of "separate customers" of member stockbrokers clearly recognize that beneficial ownership of an account is the critical factor in

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ment by the trustee that the claim is partially for securities and thus the statutory limit of \$50,000 based on a claim of securities should be applicable.

<sup>2</sup> In this case, \$20,000 since only claims for cash are involved. See Section 6(f)(1)(A) and footnote (1) *supra*.



*Memorandum Opinion of Bankruptcy Judge Babitt*

determining who is to be considered a "customer" of a stockbroker member. Thus Rule 10(b) reads as follows:

"An account held with a member by an agent or nominee for another person as a principal or beneficial owner shall, except as otherwise provided in the rules of this series, be deemed to be an individual account of such principal or beneficial owner."

Although under Subsection (c) of Rule 101 Morgan Kennedy's trustee could be required by the SIPC to provide satisfactory evidence as to the beneficial ownership of an account in the instant case, there is basically no dispute that the beneficial owners of the trust are the individual employees of the Company. I hold they must be deemed the real "customers" with respect to the account. Thus, each is entitled to the \$20,000 maximum coverage.

The SIPC advances Rules 104 to support its contention that it is the profit-sharing trust entity and not the beneficiaries which is to be considered the customer to be protected by the Act. But Rule 104 does not specifically deal with this issue. Rather, Rule 104 deals with special instances where a beneficiary or trustee *also* has an individual account with a broker-dealer subsequently liquidated pursuant to the provisions of the SIPA. Rule 104 does no more than apply the principle that accounts held in different capacities are to be considered accounts of "separate customers." In such instances the Rule provides such beneficiaries and trustees with double coverage for they are indeed separate customers. Rule 104 does not specifically treat the issue of separate coverage for the beneficiaries of a trust as a customer. Accordingly, reliance by the SIPC on Rule 104, apparently on the theory that it affords the only basis for separation of entities and no other is authorized, is misplaced.

It is also significant that the legislative history of the SIPA supports the reading of the statute that those within its reach, *i.e.*, securities investors, be provided with pro-



*Memorandum Opinion of Bankruptcy Judge Babitt*

tection comparable to that afforded by the Federal Deposit Insurance Act ("FDIA") and the Federal Savings & Loan Insurance Act ("FSLIA"). See House Report No. 91-1613, Oct. 21, 1970, in *U. S. Code Congressional and Administrative News*, 91st Cong., 2d Sess. 1970, p. 5255, where it is said that

"the need is similar, in many respects, to that which prompted the establishment of the Federal Deposit Insurance Corporation and the Federal Savings & Loan Insurance Corporation."

Under regulations adopted by the FDIC and the FSLIC each beneficiary of a trust which maintains an account at an insured institution is deemed a "separate customer" and is therefore individually entitled to protection up to the prescribed maximum. 12 C.F.R. § 330—Appendix (1973). Since neither the SIPA or the Series 100 Rules provide any specific guidance in this area and in view of the Congressional expression to provide similar coverage under the SIPA as to that provided by the FDIA and the FSLIA, the regulations of the latter provide, at the very least, a strong indication as to how separate trust interests ought to be treated under the 1970 SIPA.

It is my conclusion that each of the 108 beneficiaries should be considered a separate "customer" within the meaning of Section 6(f)(1) of SIPA, 15 U.S.C. 78fff(f)(1). In so deciding I am not unmindful of the deference normally paid to the reading given by an agency charged with applying a statute. However, any deference in overriding the SIPC's construction (opposed to that of its trustee) must be overcome where the language of the statute does not support such construction and SIPC's own rules and the legislative history suggest otherwise.

Submit an order.

Dated: New York, New York  
January 21, 1975.

/s/ ROY BABITT  
Bankruptcy Judge

*Order of Judgment of Bankruptcy Judge Babitt*

(Caption Omitted in Printing)

**Order of Judgment**

(Filed Feb. 14, 1975, Roy Babitt, Bankruptcy Judge)

Upon the application of Eugene L. Bondy, Jr., Esq., Trustee in the above-captioned matter ("Trustee"), to designate The Claim of the Trustees of the Reading Body Works Profit Sharing Plan Trust (the "Trust") as the separate claims of the 108 beneficiaries of the Trust and to declare that each such beneficiary is entitled to protection as a separate "customer" under Section 6(c)(2)(A)(ii) of the Securities Investor Protector Act, the application filed in opposition by the Securities Investor Protection Corporation, the application filed in support by the Trust and all other papers and proceedings herein, upon the memorandum opinion of this Court dated January 21, 1975, the Court having considered such submissions, and the Court having duly advised in the premises, it is

ORDERED that the claim filed by the Trustees of the Trust be and hereby is designated the separate claims of the 108 beneficiaries of the Trust and it is hereby declared that each such beneficiary is entitled to protection as a separate "customer" under Section 6(c)(2)(A)(ii) of the Securities Investor Protection Act.

Dated: New York, New York, February 14, 1975.

/s/ ROY BABITT  
Bankruptcy Judge

*Notice of Appeal to District Court*

(Caption Omitted in Printing)

**Notice of Appeal to District Court**

Securities Investor Protection Corporation, the Applicant, appeals to the district court from the order and judgment of the referee entered in this case on February 14, 1975, designating the claim filed by the trustees of the Reading Body Works Profit Sharing Plan Trust ("Trust") as the separate claims of the 108 beneficiaries of the Trust and declaring that each such beneficiary is entitled to protection as a "separate customer" under section 6(e)(2)(A)(ii) of the Securities Investor Protection Act. The parties to the judgment appealed from and the names and addresses of their respective attorneys are as follows:

Rogers & Wells, attorneys for  
Eugene L. Bondy, Jr., Esquire  
Trustee for the Liquidation of the  
Business of Morgan, Kennedy  
& Co., Inc.

200 Park Avenue  
New York, New York 10017

Charles M. Solomon, Esquire  
Attorney for Trustees of Reading  
Body Works Profit Sharing Plan  
Trust

Fox, Rothchild, O'Brien & Frankel  
1401 Walnut Street  
Philadelphia, Pennsylvania 19102



*Notice of Appeal to District Court*

Dated: February 20, 1975

/s/ THEODORE H. FOCHT  
Theodore H. Focht  
*General Counsel*

*Attorney for Appellant*  
SECURITIFS INVESTOR PROTECTION  
CORPORATION  
900 Seventeenth Street  
Suite 800  
Washington, D.C. 20006  
(202) 223-8400



(Caption Omitted in Printing)

**Memorandum**

FRANKEL, D. J.

The facts are undisputed and are outlined with characteristic lucidity by Bankruptcy Judge Babitt. The question is difficult. The statute, as a purely textual matter, favors the appellant. When the underlying policies and relevant analogies are considered, the balance tips the other way, as Judge Babitt held. Agreeing in the end with the ruling below, this court adds, or repeats, only a few observations:

1. While the statutory language on its face may favor SIPC, this must not be exaggerated. Even on this somewhat arid level, there is substantial room for debate. As SIPC stresses, the advances are provided for payments to "each customer . . ." 15 U.S.C. § 78fff(f)(1). But "customers" in turn are "persons . . . who have claims on account of securities . . . and . . . persons who have claims against the debtor arising out of sales or conversions of such securities. . . ." § 78fff(c)(2)(A)(ii). It is scarcely an unbearable wrench to include employees for whom the Trust existed as such "persons." It is in this setting that the Bankruptcy Judge deemed significant SIPC's own Rule 101(b). For the purpose embraced by that Rule SIPC found itself comfortably able to look beyond the formalities of "title" and account designations to protect the "persons" affected with the kind of substantial interest Congress cared about. The analogy, if not decisive, is sound and useful.

2. Elsewhere in its own Rules SIPC has shown that there is no undeviating identity between an "account" and a "customer"; it has overridden the identity even where the result has been to diminish the protection for individual beneficiaries. SIPC's Rule (104)(c) says that

*Memorandum Order of District Judge Marvin E. Frankel*

where more than one trust account is held for the same beneficiary "such accounts shall be combined so that the maximum protection afforded to such accounts in the aggregate shall be the maximum protection afforded to one 'separate customer' of the member." Piercing the formal designation of "accounts" in that situation, SIPC has looked at the individual human "beneficiary" as the measure of the protection. That approach should not be shunned when it is favorable to the real party in interest—the true investor with his small but vital stake—and adopted only when it hurts. The overriding purpose remains after all to effect "the speedy return of most customer property." *Securities Investor Protection Corp. v. Barbour*, 43 U.S.L.W. 4630, 4631 (May 19, 1975).

3. Acknowledging the consonance of the decision below with the Congressional purpose to afford maximum protection to the preponderant majority of small investors, SIPC nevertheless foretells disasters from Judge Babitt's ruling, extending even to threats of moment affecting the Treasury of the United States. The worry seems excessive. To be sure, the \$100,000 or so affected by this case is not *de minimis*. And there will presumably be other cases and more money. But there is no concrete suggestion as to how catastrophes will happen. SIPC itself observes that there was an apparent desire in the Congress to cover fully by the \$50,000 and \$20,000 figures the "vast majority" of investors, well in excess of 90%. Hearings on H.R. 13308, H.R. 17585, H.R. 18081, H.R. 18109, H.R. 18458 Before the Subcomm. on Commerce & Finance of the House Comm. on Interstate & Foreign Commerce, 91st Cong., 2d Sess. 379-80 (1970). We are not directed to any actuarial surprise, any concrete projection, or, certainly, any remote ground of policy for shuddering over the result herein approved.

4. We have been taught before now, at SIPC's urging, that the dryly literal definition of "customer" does not

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suffice to defeat "the patent legislative purposes." *S.E.C. v. F. O. Baroff Company, Inc.*, 497 F.2d 280, 282 (2d Cir. 1974). Though the cited case is not in point today, its familiar principle supports the result ordered by Judge Babitt. Forgetting its own employment of the principle, SIPC leans on language saying a customer must literally be one "with whom the debtor deals," 15 U.S.C. § 78 fff (c)(2)(iii), and one who is the addressee of notice that a proceeding has been commenced, § 78fff(e).<sup>\*</sup> That this proves too much is shown by referring again to SIPC's Rules.

The order of the Bankruptcy Judge is affirmed.  
So ordered.

Dated, New York, New York, June 10, 1975.

/s/ MARVIN E. FRANKEL  
U.S.D.J.

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<sup>\*</sup> Brief of Appellant 23-24.

*Notice of Appeals to the Court of Appeals*

(Caption Omitted in Printing)

**Notice of Appeal**

Notice is hereby given that Securities Investor Protection Corporation, Applicant above-named, hereby appeals to the United States Court of Appeals for the Second Circuit from the Order of District Judge Marvin E. Frankel, affirming the February 14, 1975 Order of Bankruptcy Judge Roy Babitt, entered in this action on the 10th day of June, 1975.

Dated: July 3, 1975

/s/ MICHAEL E. DON  
Michael E. Don  
*Senior Attorney*

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